CIA/OER/S-06654-74 MIDDLE EAST OIL EARNINGS & INVESTMENT
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MEMORANDUM FOR THE RECORD

SUBJECT: Middle East Oil Earnings and Investment

The attached paper, "Middle East Oil Earnings and Investment," was prepared for the use of the D/OER and NIO/EC in their briefing of the President's Foreign Intelligence Advisory Board. At their request, the paper is also being provided to members of the inter-Agency committee studying OPEC investment: Donald Curtis and Charles Schotta of Treasury, Sam Pizer of the Federal Reserve Board, Frank Vargo of the Commerce Department, and Carl Cundiff of the Department of State.

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Attachment:
As stated

Distribution: (S-6654)
1 - D/OER, SA/ER
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MIDDLE EAST OIL EARNINGS AND INVESTMENT

I. Middle East Oil Earnings

A. Oil receipts of the eight major Middle East producers will total $74 billion in 1974, almost 80% of total OPEC revenue (see Table 1).

TABLE 1

ESTIMATED MIDDLE EAST OIL RECEIPTS, 1974

(Billion US$)

	1st Half	2nd Half	1974 Total
ALGERIA	1.7	2.1	3.8
IRAN	7.0	11.2	18.2
IRAQ	2.2	2.9	5.1
KUWAIT	1.2	6.2	7.4
LIBYA	3.5	3.2	6.7
QATAR	.6	.9	1.5
SAUDI ARABIA	7.4	17.2	24.6
UNITED ARAB EMIRATES	1.8	4.7	6.5
TOTAL	25.4	48.4	73.8

B. Oil revenues would have been even greater were it not for the lag between the time oil is produced and the time it is paid for.

1. Normal payments are lagged on the average two to three months.

2. Special deferrals were allowed by some producers duirng the first half of the year while negotiations on new participation arrangements were in progress.

C. If payments were made concurrently with production, revenues would total about $87 billion this year (see Table 2).

TABLE 2

ESTIMATED MIDDLE EAST ACCRUED OIL EARNINGS, 1974

	(Billion US$)
ALGERIA	4.1
IRAN	20.3
IRAQ	5.8
KUWAIT	8.6
LIBYA	6.7
QATAR	1.9
SAUDI ARABIA	29.9
UNITED ARAB EMIRATES	9.6
TOTAL	86.9

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D. The lag in payments shifted the impact of higher oil prices to the second half of the year.

1. Monthly receipts in the first quarter of 1974 averaged $2.9 billion.

2. Monthly receipts in the second quarter averaged $5.6 billion.

3. Monthly receipts in the second half of the year are averaging $8.0 billion.

E. Oil revenues will be concentrated in relatively few countries -- Saudi Arabia and Iran will receive $43 billion, or nearly 60% of total Middle East oil earnings.

F. If oil prices continue at present levels, the monthly receipts of Middle East oil producers will average about $6.8 billion in 1975.

1. Even if recent price increases announced by some Persian Gulf producers are widely adopted, Middle East producers receipts will drop by about $1.5 billion a month from present levels.

II. Middle East Imports

A. Middle East oil producers will be hard pressed to spend more than a small fraction of their growing wealth.

B. Total import expenditures (f.o.b.) are only expected to reach $22 billion, or less than 30% of projected oil earnings in 1974 (see Table 3).

TABLE 3

ESTIMATED MIDDLE EAST IMPORTS (f.o.b.), 1974

(Billion US$)

ALGERIA	3.5
IRAN	6.9
IRAQ	2.3
KUWAIT	1.4
LIBYA	2.6
QATAR	.2
SAUDI ARABIA	3.3
UNITED ARAB EMIRATES	1.3
TOTAL	21.5

C. Preliminary estimates indicate that imports will probably exceed $30 billion in 1975, still less than 40% of projected oil earnings.

D. Low absorbers include Saudi Arabia, Qatar, and the United Arab Emirates (see Table 4).

1. With small populations and limited domestic investment opportunities, the earnings of these nations exceeded their ability to absorb foreign goods and services even before the oil price increases.

E. High absorbers include Algeria, Iran, Iraq, and Libya.

1. For the most part, these countries have large populations and greater opportunities for internal development. Nevertheless, in the short run, revenue increases are outstripping absorptive ability even in these countries.

TABLE 4

ABSORPTIVE CAPACITY OF MIDDLE EAST PRODUCERS, 1974:
IMPORTS AS A PERCENT OF OIL REVENUES

	(Percent)
ALGERIA	92
IRAN	38
IRAQ	45
KUWAIT	19
LIBYA	39
QATAR	13
SAUDI ARABIA	13
UNITED ARAB EMIRATES	20
AVERAGE	29

III. Middle East Investable Surplus

A. Preliminary estimates indicate the Middle East oil producers will accumulate an investable surplus of about $52 billion this year (see Table 5).

TABLE 5

ESTIMATED MIDDLE EAST INVESTABLE SURPLUS, 1974

(Billion US$)

Export Receipts	75.3
Oil	73.8
Non-Oil	1.5
Import Payments (f.o.b.)	21.5
Net Services	-1.6
Investable Surplus	52.2

B. Foreign aid will reduce the investable surplus in 1974 by not more than $4 billion.

1. The Middle East oil producers' current account surplus will consequently be in excess of $48 billion.

IV. Middle East Investment Patterns

A. Producers have continued to place the bulk of their investable surplus in financial markets in a few developed countries.

B. The basic investment objectives of the Middle East oil producers include:

- Insuring their holding against political seizure.
- Maintaining -- and, if possible, increasing -- the real value of their assets.
- Retaining effective control of their investments.

C. Most holdings are dollar denominated (see Table 6).

1. Eurodollar investments -- dollar assets outside the United States -- make up about 40% of the total.
2. Dollar holdings in the United States account for an additional 15%.

TABLE 6

CURRENCY DENOMINATION OF OFFICIAL FOREIGN ASSETS OF MIDDLE EAST OIL PRODUCERS, 30 SEPTEMBER 1974

(Percent)

EURODOLLARS	40
US DOLLARS	15
STERLING	15
OTHER CURRENCIES	25
GOLD AND RESERVE POSITION IN THE IMF	5
TOTAL FOREIGN ASSETS	38 Billion US$

D. Most Middle East holdings are in liquid assets, particularly bank deposits (see Table 7).

1. These deposits are safe, easily managed, and can be readily channeled through intermediaries to provide the anonymity that makes seizure unlikely.

TABLE 7

COMPOSITION OF OFFICIAL FOREIGN ASSETS
OF MIDDLE EAST OIL PRODUCERS

(Percent)

	30 Sept 1974
GOLD AND RESERVE POSITION IN THE IMF	5
OTHER FOREIGN RESERVES	85
BANK DEPOSITS	60
TREASURY STOCKS AND BONDS	10
SELECTED NOTES AND LOANS	15
OTHER FOREIGN ASSETS, INCLUDING EQUITIES AND REAL ESTATE	10
TOTAL FOREIGN ASSETS	38 Billion US$

E. The concentration of Arab investments is straining the Eurodollar market. Eurodollar banks, reluctant to accept oil money on terms that producers desire, now offer somewhat lower-than-market rates on these deposits.

1. At present, the US financial market is the only other market in which producers can realize their investment goals.

2. The US financial market, because of its size and depth, will probably continue to receive a growing share of producer deposits.

F. The share of Middle East investments placed in the United States has increased through 1974.

1. 16% of observed Middle East investment was placed in the United States during the first quarter of 1974.

2. 17% and 27% of observed investments were placed in the United States during the second and third quarters, respectively.

G. As import expenditure rise, problems arising from the oil producers' accumulation of wealth will gradually shift.

1. The producers' investable surplus will decline both absolutely and relative to world trade and production.

2. Foreign holdings will become increasingly concentrated in Saudi Arabia, Kuwait, and the Arab Persian Gulf states.
3. Longer-term assets will increase in importance as the relative size of bank deposits decline.
4. An increasing share of producer wealth will be placed in US financial markets.

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